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REGAL REAL ESTATE INVESTMENT TRUST

(a Hong Kong collective investment scheme authorised under section 104 of the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong))

(Stock Code: 1881)

Managed by



SUMMARY OF MARKET RENTAL PACKAGE OF ICLUB SHEUNG WAN HOTEL IN RESPECT OF THE 2019 LEASE YEAR

Reference is made to the announcements dated 16 November 2016 and 4 October 2017 issued by Regal REIT. In accordance with the Lease Agreement, the Valuer was jointly appointed by the Lessor and the Lessee and was instructed to conduct a rent review to determine the Market Rental Package for 2019 for the iclub Sheung Wan Hotel, which includes the amount of market rents (including Base Rent, Variable Rent and the Lessee's contribution to the FF&E Reserve) and the amount of the Security Deposit.

According to the 2019 Market Rental Package Determination, the amount payable by the Lessee as Base Rent is HK\$46.0 million for the 2019 Lease Year (an increase of HK\$4.0 million as compared with the Base Rent of HK\$42.0 million for the 2018 Lease Year under the 2018 Market Rental Package Determination). The Variable Rent will be based on the same sharing ratio of 50% of the NPI Excess for the 2019 Lease Year. For the 2019 Lease Year, the Valuer determined that, consistent with the 2018 Market Rental Package Determination, no contribution by the Lessee to the FF&E Reserve will be required. The Lessor will maintain the FF&E Reserve with an amount equivalent to 2% of the Total Hotel Revenue for each calendar month during the Second Lease Period. The Security Deposit comprised within the 2019 Market Rental Package Determination is HK\$11.751 million, as compared with the Security Deposit of HK\$10.775 million comprised within the Market Rental Package for 2018. Summaries of the 2019 Market Rental Package Determination and the valuation methodologies are set out in this announcement. The manner of payment of each component of the 2019 Market Rental Package Determination will be consistent with that set out in the 2018 Market Rental Package Determination.

The total distributable income (“**TDI**”) available for distribution to Unitholders and the distribution per Unit for each financial year are affected by various factors including, most importantly, the total rental and hotel income receivable by Regal REIT from all its hotel properties for such financial year. For the six months ended 30 June 2018, the aggregate Base Rent and Variable Rent derived from the iclub Sheung Wan Hotel amounted to HK\$22.1 million, representing approximately 4.5% of the total rental and hotel income of Regal REIT in the same period. Pursuant to the 2019 Market Rental Package Determination, there will be an increase of HK\$4.0 million in the Base Rent for the 2019 Lease Year as compared to that in the 2018 Market Rental Package Determination. Furthermore, the TDI may be subject to increase in the event that Variable Rent is receivable by the Lessor in the 2019 Lease Year. As at 30 June 2018, the valuation of the iclub Sheung Wan Hotel was HK\$1,590 million, representing 5.99% of the total valuation of HK\$26,553 million of Regal REIT’s properties portfolio.

Given the variables involved in the determination of the Base Rent and Variable Rent from year to year, investors should exercise caution in dealing in the units of Regal REIT.

Pursuant to 5.2(f) of the REIT Code, the Valuer's report on the Market Rental Package for 2019 is available for inspection by the public during normal office hours at the REIT Manager's place of business at Unit No. 2001, 20th Floor, 68 Yee Wo Street, Causeway Bay, Hong Kong.

The INEDs confirm that the rent review in respect of the 2019 Market Rental Package Determination has been conducted in accordance with the terms of the Lease Agreement. The Lessee and the Hotel Manager are connected persons of Regal REIT.

A. BACKGROUND INFORMATION TO LEASE TERM AND RENTAL INCOME STRUCTURE

Reference is made to the announcements dated 16 November 2016 and 4 October 2017 issued by Regal REIT. Unless otherwise defined herein, capitalised terms used in this announcement shall have the same meanings ascribed to them in the announcement dated 16 November 2016.

B. APPOINTMENT OF VALUER

In accordance with the Lease Agreement, Mr. David Faulkner was jointly appointed as an independent professional property valuer (the "**Valuer**") and was instructed on 27 June 2018 to conduct a rent review to determine the Market Rental Package in respect of the 2019 Lease Year for the iclub Sheung Wan Hotel (the "**Market Rental Package for 2019**"), based on the assumptions and disregards provided in the Lease Agreement. Mr. Faulkner had been jointly appointed as the Valuer to determine the Market Rental Package for the iclub Sheung Wan Hotel for the period from 10 February 2017 to 31 December 2017 and the 2018 Lease Year. He was also jointly appointed as the Valuer to determine the market rental package for the Initial Hotel Properties from 2011 to 2019 and the market rental package for the iclub Fortress Hill Hotel for the period from 28 July 2017 to 31 December 2018 and the 2019 Lease Year, which are all held by Regal REIT. Mr. Faulkner is a Chartered Surveyor with over 35 years' experience in the valuation of properties of this magnitude and nature and over 30 years' experience in Hong Kong and China, and is currently a managing director at Colliers International (Hong Kong) Limited, which is the current principal valuer of Regal REIT.

Mr. Faulkner issued his report (the “**Report**”) on the determination of the Market Rental Package for 2019 for the iclub Sheung Wan Hotel (the “**2019 Market Rental Package Determination**”) on 27 September 2018.

C. THE 2019 MARKET RENTAL PACKAGE DETERMINATION

1. Summary of the 2019 Market Rental Package Determination

A summary of the 2019 Market Rental Package Determination, together with the corresponding components in respect of the Market Rental Package for 2018, are as follows:

<u>Market Rental Package component</u>	<u>Market Rental Package for 2019</u>	<u>Market Rental Package for 2018</u>
Base Rent ⁽¹⁾	HK\$46.0 million	HK\$42.0 million
Variable Rent ⁽²⁾	50% of NPI Excess	50% of NPI Excess
Lessee’s contribution to the FF&E Reserve ⁽³⁾	No contribution by the Lessee	No contribution by the Lessee
Amount of Security Deposit ⁽⁴⁾	HK\$11.751 million	HK\$10.775 million

Notes:

- (1) The Base Rent of HK\$46.0 million for the 2019 Lease Year represents an increase of HK\$4.0 million (equivalent to an increase of 9.5%) as compared with the Base Rent of HK\$42.0 million for the 2018 Lease Year.
- (2) For the six months ended 30 June 2018, as the Net Property Income from hotel operations of the iclub Sheung Wan Hotel amounted to approximately HK\$23.3 million, which was above the prorated Base Rent amount of HK\$21.0 million, Variable Rent of HK\$1.1 million was receivable for the period. Likewise, pursuant to the 2019 Market Rental Package Determination, the Variable Rent receivable for the 2019 Lease Year will be based on the same sharing ratio of 50% of the NPI Excess for the 2019 Lease Year.

- (3) According to the Lease Agreement, the Lessee was required to, at its own costs and expense, pay to the Lessor on a monthly basis during the First Lease Period the actual costs of any FF&E disbursed. Thereafter, the Lessor is obligated to maintain the FF&E Reserve with an amount, equivalent to 2% of the Total Hotel Revenue for the preceding calendar month, to be set aside monthly during the Second Lease Period. Further, as part of the review for each Lease Year, the Valuer may determine the percentage of the Total Hotel Revenue, as part of or in addition to the aforesaid amount set aside, which the Lessee is obligated to contribute. According to the Report, as a general practice of the hotel industry in Hong Kong, the owner of the hotel (equivalent to the Lessor in the Lease Agreement) is responsible for contributing to funds which are set aside and applied to meet the costs of investments in the replacement of furniture, fixtures and equipment at the relevant hotel premises, for the purposes of maintaining such premises at the applicable operating standards and operating capacity. The Valuer was, therefore, of the opinion that the obligation to contribute to the FF&E Reserve could be transferred from the Lessee to the Lessor based on local practice and, consistent with the 2018 Market Rental Package Determination, concluded in the 2019 Market Rental Package Determination that none of the Total Hotel Revenue shall be contributed by the Lessee to the FF&E Reserve for the 2019 Lease Year.
- (4) Pursuant to the Lease Agreement, the amount of the security deposit shall be equal to the higher of: (a) the amount which the Valuer determines to be the market rate of security deposit upon market rental review; and (b) three months' Base Rent, rates and Government rent. According to the 2019 Market Rental Package Determination, the Valuer determined that the market rate of security deposit to be three months' Base Rent. Accordingly, the Security Deposit for the iclub Sheung Wan Hotel is HK\$11.751 million, equivalent to (b) above, such amount being the higher of (a) and (b).

2. Manner of Payment

The manner of payment of the Base Rent, Variable Rent, Security Deposit and the Lessee's contribution to the FF&E Reserve according to the 2019 Market Rental Package Determination will be consistent with that set out in the 2018 Market Rental Package Determination. For the 2018 Lease Year, the Lessee has procured and provided a third party guarantee (in the form of a standby letter of credit issued by a licensed bank in Hong Kong) for a security deposit amount equivalent to 3 months' Base Rent, rates and Government rent, effective on 1 January 2018. Similarly, for the 2019 Lease Year, the Lessee will procure and provide a third party guarantee (in the form of a standby letter of credit issued by a licensed bank in Hong Kong) for a security deposit amount equivalent to 3 months' Base Rent, rates and Government rent, effective on 1 January 2019.

D. PERFORMANCE OF ICLUB SHEUNG WAN HOTEL

The net property income derived from the iclub Sheung Wan Hotel for the six months ended 30 June 2018 was HK\$23.3 million (for the year ended 31 December 2017: HK\$42.1 million). For the six months ended 30 June 2018, the iclub Sheung Wan Hotel achieved an overall occupancy rate of 93.1% (for the year ended 31 December 2017: 93.7%) with an average room rate of approximately HK\$914 (for the year ended 31 December 2017: approximately HK\$864).

E. SUMMARY OF ASSUMPTIONS AND OUTLINE OF VALUATION METHODOLOGIES

1. Assumptions Contained in the 2019 Market Rental Package Determination

The 2019 Market Rental Package Determination was based on the assumptions and disregards set out in the Lease Agreement, including the following:

- (a) that the rental payable by the Lessee shall be exclusive of rates, government rent, utility charges and all other outgoings payable by the Lessee;
- (b) that the iclub Sheung Wan Hotel is available to let on the open market by a willing landlord to a willing tenant without a premium and with vacant possession having regard to similar premises having similar characteristics and attributes;
- (c) that the length of the lease would be in line with other leases in the market with similar nature;
- (d) that the iclub Sheung Wan Hotel is fit for immediate occupation and use and incorporates fixtures and fittings which are of a standard and description commensurate with the nature of the premises and which are suitable for the use and occupation of the willing tenant;
- (e) that in case any part of the iclub Sheung Wan Hotel has been damaged or destroyed, it has been fully restored;
- (f) that no reduction is to be made to take account of any inducements;
- (g) disregarding any effect on rent of the fact that the Lessee has been or is in occupation of the iclub Sheung Wan Hotel or any part thereof; and
- (h) disregarding any goodwill attributable to the Lessee's business carried on at the iclub Sheung Wan Hotel.

2. Outline of Valuation Methodologies

The Valuer adopted a reasonable percentage of gross revenue as his primary approach in his valuation to determine the Base Rent comprised within the 2019 Market Rental Package Determination. The Valuer also analysed similar sales transactions in Hong Kong to assess the market value of the iclub Sheung Wan Hotel, and Base Rent was then derived from the adoption of what the Valuer determined to be appropriate yields on such market values. As the Valuer was of the view that rental transactions of hotels are rare in Hong Kong, rental transactions of upper commercial premises were also analysed as a cross-check and benchmark for the purposes of the 2019 Market Rental Package Determination. The Valuer, being appointed and instructed jointly by the Lessor and the Lessee to conduct the Market Rental Package for 2019, determined the Variable Rent for the 2019 Lease Year to be 50% of the NPI Excess, which is a reasonable and fair proportion to both parties.

F. CONSIDERATIONS IN RESPECT OF THE MARKET RENTAL PACKAGE FOR 2019

1. Rental Review in respect of the Market Rental Package for 2019 and General Market Conditions

As previously highlighted in the Circular, the profitability of hotel business is cyclical and sensitive to changes in the global, regional or local economy generally; and since demand for hotel services in Hong Kong is affected by economic growth, a global, regional or local recession could lead to downturns which, in turn, may affect the hotel industry. Other adverse factors outside the control of Regal REIT and the Hotel Manager could include geopolitical tensions, natural disasters, changes in law and other events (such as a slowdown in the growth of number of mainland Chinese visitor arrivals to Hong Kong pursuant to the People's Republic of China's Individual Visit Scheme) which may impact negatively on the tourism industry and hotel business, including hotel bookings and the food and beverage business at hotels in Hong Kong. The occurrence of one or more of these events may have an adverse effect on the operating performance of the iclub Sheung Wan Hotel, the Lessee and, ultimately, Regal REIT.

Driven by the continuing global recovery, the relatively low interest rate environment and the buoyant property market, the economy in Hong Kong is likely to maintain a growing trend in the second half of 2018. However, the recent trade disputes between the United States and China are casting significant uncertainties on the global economy and if these international trade disputes and other geopolitical tensions escalate, they could have serious dampening effect on economic growth globally.

The rental levels that may be obtained during the Second Lease Period will principally depend on the prevailing market conditions at that time.

The Base Rent and the Variable Rent comprised within the 2019 Market Rental Package Determination has been based on the Valuer's professional assessment on the market environment for 2019 (taking into account the assumptions and disregards set out in paragraph E.1 above) and other factors relating to the iclub Sheung Wan Hotel, and with reference to the current market conditions and outlook of the hotel and tourism industry in Hong Kong. The adoption of having the Base Rent, plus potential upside sharing through Variable Rent in accordance with the Lease Agreement, provides assurance of a relatively stable rental income from the iclub Sheung Wan Hotel for Regal REIT for the 2019 Lease Year.

Based on the number of factors and hotel business conditions as mentioned above, there is an increase of 9.5% in the Base Rent determined for the 2019 Lease Year, as compared with the Base Rent of HK\$42.0 million for the 2018 Lease Year.

2. Impact on Total Distributable Income and Distribution per Unit

The Base Rents in respect of each of the Lease Years within the Second Lease Period will be determined in accordance with an annual rent review by a jointly appointed independent professional property valuer and will be more reflective of the prevailing market conditions at the time each annual rental review is conducted.

The TDI available for distribution to Unitholders and the distribution per Unit for each financial year is affected by various factors including, most importantly, the total rental and hotel income receivable by Regal REIT from all its hotel properties for such financial year. For the six months ended 30 June 2018, the aggregate Base Rent and Variable Rent derived from the iclub Sheung Wan Hotel amounted to HK\$22.1 million, representing approximately 4.5% of the total rental and hotel income of Regal REIT in the same period. Pursuant to the 2019 Market Rental Package Determination, there will be an increase of HK\$4.0 million (equivalent to an increase of 9.5%) in the Base Rent for the 2019 Lease Year as compared to that in the 2018 Market Rental Package Determination. Furthermore, the TDI may be subject to increase in the event that Variable Rent is receivable by the Lessor in the 2019 Lease Year. As at 30 June 2018, the valuation of the iclub Sheung Wan Hotel was HK\$1,590 million, representing 5.99% of the total valuation of HK\$26,553 million of Regal REIT's properties portfolio.

Given the variables involved in the determination of the Base Rent and the Variable Rent from year to year, investors should exercise caution in dealing in the units of Regal REIT.

G. INSPECTION OF VALUER'S REPORT

Pursuant to 5.2(f) of the REIT Code, the Valuer's report on the Market Rental Package for 2019 is available for inspection by the public during normal office hours at the REIT Manager's place of business at Unit No. 2001, 20th Floor, 68 Yee Wo Street, Causeway Bay, Hong Kong.

H. CONFIRMATION BY THE INEDs

The INEDs confirm the following:

- (a) the Board (including all of the INEDs) (other than Mr. LO Yuk Sui, Miss LO Po Man, Mr. Donald FAN Tung, Mr. Jimmy LO Chun To, Mr. Kenneth NG Kwai Kai and Hon. Abraham SHEK Lai Him, GBS, JP, who were deemed to have interests in the Transaction Matters Requiring Approval) at the time of the Circular had confirmed that the terms of agreements (including the Lease Agreement) in respect of iclub Sheung Wan Hotel referred to in the section headed "Continuing Connected Transactions" of the Circular were entered into in the ordinary and usual course of business of Regal REIT, and on terms which are normal commercial terms, at arm's length and are fair and reasonable and in the interests of the Independent Unitholders, as well as the Unitholders as a whole;
- (b) the Board (including all of the INEDs) (other than Mr. LO Yuk Sui, Miss LO Po Man, Mr. Donald FAN Tung, Mr. Jimmy LO Chun To, Mr. Kenneth NG Kwai Kai, Mr. Bowen Joseph LEUNG Po Wing, GBS, JP and Hon. Abraham SHEK Lai Him, GBS, JP, who were deemed to have interests in the Transaction Matters Requiring Approval) had further confirmed that the Lease Agreement continues to be conducted in the ordinary and usual course of business and the terms of the Lease Agreement are at arm's length, on normal commercial terms and are fair and reasonable and in the best interests of the Independent Unitholders, as well as the Unitholders as a whole;
- (c) the appointment of Mr. David Faulkner as the independent professional property valuer for the 2019 Market Rental Package Determination has been reviewed, considered and endorsed by the Audit Committee of the REIT Manager; and

- (d) the rent review in respect of the 2019 Market Rental Package Determination has been conducted in accordance with the terms of the Lease Agreement.

A summary of the 2019 Market Rental Package Determination will be disclosed in the interim and annual reports of Regal REIT for the financial period ending 30 June 2019 and the financial year ending 31 December 2019, respectively.

This announcement is made pursuant to Chapter 10 of the REIT Code.

DEFINITIONS

In this announcement, unless the context otherwise requires, the following terms have the following meanings:

- “Hotel Manager” means Regal Hotels International Limited, a wholly-owned subsidiary of Regal and a connected person of Regal REIT;
- “INEDs” means the independent non-executive directors of the REIT Manager;
- “Initial Hotel Properties” means Regal Airport Hotel, Regal Hongkong Hotel, Regal Kowloon Hotel, Regal Oriental Hotel and Regal Riverside Hotel, which are wholly-owned by Regal REIT;
- “Lease Agreement” means Lease Agreement for the iclub Sheung Wan Hotel entered into between the Lessor and the Lessee on 10 February 2014;
- “Lease Year” means (a) each of the first three one-year periods of the term of the Lease Agreement; (b) the period commencing immediately following the end of the third one-year period of the term of the Lease Agreement and ending on 31 December of the same calendar year; and (c) each calendar year immediately following the end of period described in (b) above;
- “Lessee” means Favour Link International Limited, a wholly-owned subsidiary of Regal and a connected person of Regal REIT;
- “Lessor” means Tristan Limited, the direct owner of the iclub Sheung Wan Hotel and a wholly-owned subsidiary of Regal REIT;

- “NPI Excess” means Net Property Income (as defined in the Circular) for a Lease Year exceeds the Base Rent for the same Lease Year;
- “Regal” means Regal Hotels International Holdings Limited, a company incorporated in Bermuda with limited liability, whose shares are listed on the main board of The Stock Exchange of Hong Kong Limited (Stock Code: 78) and a connected person of Regal REIT; and
- “REIT Manager” means Regal Portfolio Management Limited, as the manager of Regal REIT.

By Order of the Board
Regal Portfolio Management Limited
(as manager of Regal Real Estate Investment Trust)
Simon LAM Man Lim
Executive Director

Hong Kong, 5 October 2018

As at the date of this announcement, the Board comprises Mr. LO Yuk Sui as Chairman and Non-executive Director; Miss LO Po Man as Vice Chairman and Non-executive Director; Mr. Johnny CHEN Sing Hung and Mr. Simon LAM Man Lim as Executive Directors; Mr. Donald FAN Tung, Mr. Jimmy LO Chun To and Mr. Kenneth NG Kwai Kai as Non-executive Directors; and Mr. John William CRAWFORD, JP, Mr. Bowen Joseph LEUNG Po Wing, GBS, JP, Mr. Kai Ole RINGENSON and Hon. Abraham SHEK Lai Him, GBS, JP as Independent Non-executive Directors.